No. 311

In The

Supreme Court of the United States

October Term, 1957

Commissioner of Internal Revenue,
Petitioner,

v.

Jean F. Stern,
Respondent, Transferee.

On Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit

RESPONDENT'S BRIEF

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INDEX

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RESPONDENT'S BRIEF

Respondent agrees with the presentation of the petitioner under the following headings:

OPINIONS BELOW

JURISDICTION

STATUTES AND REGULATIONS INVOLVED

Respondent relies upon the following statutes in addition to those printed in petitioner's brief at pp. 42-49:

(INTERNAL REVENUE CODE)

SEC. 811(a). DECEDENT'S INTEREST.

To the extent therein of the decedent at the time of his death;

SEC. 1119(a). BURDEN OF PROOF.

In proceedings before the Board the burden of proof shall be upon the Commissioner to show that a petitioner is liable as a transferee of property of a taxpayer, but not to show that the taxpayer was liable for the tax.

SEC. 3670. PROPERTY SUBJECT TO LIEN.

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, penalty, additional amount, or addition to such tax, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.

SEC. 3671. PERIOD OF LIEN.

Unless another date is specifically fixed by law, the lien shall arise at the time the assessment list was received by the collector and shall continue until the liability for such amount is satisfied or becomes unenforceable by reason of lapse of time.

(UNITED STATES CODE)

TITLE 28, SEC. 1652.

The laws of the several states, except where the Constitution or treaties of the United States or Acts of Congress otherwise require or provide, shall be regarded as rules of decisions in civil actions in the courts of the United States, in cases where they apply. (June 25, 1948, c. 646, 62 Stat. 944.)

QUESTIONS PRESENTED

The questions presented in the petition for certiorari were as follows:

"1. Whether respondent is liable, under Section 311 of the Internal Revenue Code of 1939, as a transferee of the cash surrender values of the policies.

"2. Whether, more broadly, respondent is liable as a transferee, under the same section of the Code, to the full extent of the net proceeds of the policies."

Respondent submits that the following additional questions are involved:

3. Whether respondent's liability as transferee of decedent may properly be considered by this Court, when the only issue presented to and decided by The Tax Court was respondent's liability as transferee of the decedent's estate.

4. Whether respondent's liability as transferee with respect to the cash surrender values of the policies may properly be considered by this Court, when the only issue presented to and decided by The Tax Court was respondent's liability as transferee with respect to the proceeds of insurance.

STATEMENT

Respondent agrees with the statement of petitioner, except the following should be added to it, inasmuch as petitioner has the burden of proof with respect to transferee liability:

> There was no evidence and no finding of insolvency as of any date prior to decedent's death; and there was no evidence or finding that decedent took out or maintained the policies with intent to hinder, delay or defraud creditors. (CA Opinion, R. 18.) There was no evidence or finding that decedent paid any of the premiums on the insurance policies during any

of the years with respect to which deficiencies in income taxes were determined or during any of the years subsequent thereto.

SUMMARY OF ARGUMENT

I

Respondent's liability for the unpaid income taxes of decedent depends upon:

(1) Whether the proceeds or cash surrender values were the property of the deceased;

(2) Whether respondent is a transferee of the proceeds or cash surrender values within the meaning of Sec. 311; and

(3) Whether respondent is liable at law or in equity, assuming that she is a transferee.

The proceeds of insurance belonged to the insurance companies and never belonged to the decedent. The proceeds were paid to the respondent pursuant to contracts of insurance, under which decedent agreed to pay the premiums in consideration of the promises of the companies to pay the proceeds to respondent upon decedent's death. That an insurance company pays its own money when it pays the proceeds is evident from the fact that the proceeds are payable upon the death of the insured even though his death may occur immediately after the policy becomes effective.

The Court below in *Stern*, The Second Circuit in *Rowen*, the Third Circuit in *Bess*, the Fifth Circuit in *Truax*, and the Seventh Circuit in *New*, all held that proceeds of insurance do not belong to the insured, and no Court of Appeals has held to the contrary. The Tax Court has been alone in so holding.

Decisions upholding the includibility of proceeds of insurance in the gross estate for estate purposes are not apposite. An analysis of Sec. 811 shows that Congress

did not consider the decedent to have an interest in proceeds of insurance at the time of his death, otherwise they would be includible under Sec. 811(a) and it would not be necessary to include them specifically in Sec. 811(g). The distinction between the interest of a decedent in property and the interest of a beneficiary in proceeds of insurance is recognized by the Courts.

Inasmuch as the proceeds of insurance did not belong to decedent during his lifetime, respondent was not a transferee of property of the decedent with respect to the proceeds. The Court below and the other Circuits referred to above held to this effect.

II

Under the contracts of insurance, decedent was required to pay the premiums in consideration of the insurance companies' promises to pay the proceeds to respondent after his death. The laws of the various states require insurance companies to maintain a reserve for solvency purposes. This reserve is made up of a portion of the level premiums paid by a large group of policyholders, together with interest thereon, and the cash surrender value of a particular policy is considered equitably to be a proratable part of the reserve. If the premiums paid by the insured belong to the companies and never belong to him, and the reserve fund is made up in part of premiums and in part with interest earned thereon, it follows that the cash surrender values never belong to the insured, as they are considered to be a proratable portion of the reserve. If the insured were the owner of the reserve or the cash surrender values, he would have to pay an income tax on the interest accruing in the reserve, and, moreover, he would not be required to pay interest to the company on any loan obtained upon the security of his policies.

Decisions growing out of the Bankruptcy Act are not controlling on the question of whether an insured owns the cash surrender values of his policies, as that Act specifically provides that powers exercisable by the bankrupt for his own benefit devolve upon the trustee. These cases hold that the power of the bankrupt insured to surrender his policy for the cash surrender value is a power devolving upon the trustee; but they do not hold that the bankrupt owns the cash surrender value of his policy.

Decisions involving liens perfected during the decedent's lifetime likewise are not apposite to the question involved herein. Federal tax liens apply to property and to interests of property of the taxpayer. Policies of insurance are property of the taxpayer, and, consequently, the lien applies to them. Liens follow property *cum onere*, and, hence, the Courts have held that the Government is entitled to recover from the beneficiary an amount equal to the value of the policies represented by their cash surrender values at the time of the decedent's death.

The Court below held that the deceased never owned the cash surrender values during his lifetime, and, consequently, that respondent was not a transferee with respect thereto within the meaning of Sec. 311. The Second Circuit in *Rowen* and the Third Circuit in *Bess*, however, held that the decedent owned the cash surrender values during his lifetime and that they merged in the proceeds at the time of his death. This result seems to be incompatible with their unqualified holding that the proceeds always belonged to the companies and never belonged to the insured. If the cash surrender values belonged to the insured during his lifetime and the proceeds always belonged to the companies, it is somewhat difficult to rationalize how property always belonging to the decedent can merge with property always belonging to the companies and still retain its identity in the hands of the beneficiary.

III

Even though respondent were a transferee of the proceeds or of the cash surrender values, she had no liability as a transferee. There is no Federal statute determining the liability of a transferee under Sec. 311, and, accordingly, it is necessary to look to the law of the State, in this case Kentucky.

The Kentucky courts have held that the purpose of the Kentucky Revised Statutes, Secs. 297.140 and 297.150 is to give a married woman a separate estate in the proceeds free from the debts of her husband, the insured; that she has more than a mere expectancy in the proceeds; that it is a right which is subject to be defeated by the insured by changing the beneficiary; and that in the event of her death before the insured, her executor is entitled to the proceeds in the absence of any change in the beneficiary prior to the insured's death.

The Court below discussed the law of Kentucky applicable to insurance polices, but did not rely upon it in view of the Court's holding that the respondent was not a transferee of either the proceeds or the cash surrender values of the policies.

The Second Circuit in *Rowen* and the Fifth Circuit in *Truax* held that State law governed and that under the applicable law of New York and Georgia, respectively, the beneficiary was not liable as a transferee. These laws are in practically the language as the law of Kentucky. The Third Circuit in *Bess* held that the law of New Jersey, which also is practically the same as the law of Kentucky, gave the wife beneficiary a vested interest; but that Court held that the general law as interpreted by Federal Courts applied, not the State law,—without, however, pointing out the general law which rendered the beneficiary liable as a transferee.

In any event, petitioner has the burden of proving that respondent is liable as a transferee of property of the decedent; and this petitioner has failed to do.

IV

The only question before the Tax Court was respondent's liability as a transferee of the decedent's estate with respect to the proceeds of insurance. No issue was raised as to her liability as a transferee of the decedent or regarding her liability with respect to the cash surrender values of the policies. These questions are not properly before this Court.

ARGUMENT

Although respondent contends that the questions presented in the petition for certiorari may not properly be considered by this Court in so far as they apply to the cash surrender values of the policies or with respect to respondent's liability as a transferee of decedent for the reason that they were not presented to or decided by The Tax Court, respondent's argument will be addressed, *first*, to the questions discussed in respondent's brief, and, *second*, to respondent's contention that issues not presented to or decided by The Tax Court are not properly before this Court.

POINT I

Respondent Is Not A Transferee of the Proceeds

Two questions arise under Sec. 311(a)(1), I.R.C. of 1939:

1. Whether respondent is "a transferee of property of a taxpayer;" and

2. Assuming that she is a transferee, whether she has any "liability, at law or in equity." (Pet. Br. 42.)

The first of these questions logically is divisible into two parts:

(1) Were the proceeds of insurance the *property of a taxpayer,* viz., the deceased insured?

(2) Was respondent a *transferee* of the proceeds *within the meaning of Sec. 311(a)(1)?*

1. *The Proceeds Were Not The Property of A Taxpayer*

In Krueger and Waggoner, "The Life Insurance Policy Contract," 1953 Edition, published by The American Society Of Chartered Life Underwriters, the following statement is made with respect to the nature of a life insurance policy:

> "An insurance policy is a contract under which the company agrees that, in consideration of certain payments to it by the policyholder, it will pay a specified amount to the beneficiary at the insured's death. It is not paying the beneficiary the insured's property, but is paying its own funds which are not traceable to any funds received from the policyholder and may be greatly in excess thereof.[1] A beneficiary under an insurance policy is likened to the 'third-party beneficiary' known in other forms of contract law." (P. 83.)

Every Court of Appeals which has passed upon the question to date has held that proceeds of life insurance payable to an individual beneficiary after the death of the insured never belonged to the insured during his lifetime or to his estate after his death, (*Stern* v. *Comm.*, R. 17; 242 F (2d) 322 (CA 6th, 1957); *Tyson* v. *Comm.*, 212 F (2d) 16 (CA 6th, 1954); *Rowen* v. *Comm.*, 215 F (2d) 641 (CA 2nd, 1954); *U. S.* v. *New*, 217 F (2d) 166 (CA 7th, 1954); *U. S.* v. *Truax*, 233 F (2d) 229 (CA 5th, 1955);

[1] For instance, the entire proceeds become payable upon death, even though death may occur immediately after the policy becomes effective.

U. S. v. *Bess*, 243 F (2d) 675 (CA 3rd, 1957), pending on certiorari, Nos. 395 and 410).[2]

Petitioner admits that these cases are against him, but he relies upon the following cases upholding the imposition of the estate tax upon the transfer of proceeds of life insurance to an individual beneficiary, where the insured retains the right to change the beneficiary until the date of his death (Pet. Br. 13-15); (*Chase Nat. Bank* v. *U. S.*, 278 U. S. 327, 73 L. Ed. 405, 49 S. Ct. 126 (1929); *Heiner* v. *Grandin*, 44 F (2d) 141 (CCA 3rd, 1930), aff'd on reargument, 56 F (2d) 1082 (1932), cert. den. 286 U. S. 561, 76 L. Ed. 1294, 52 S. Ct. 643 (1932); *Cook* v. *Comm.* 66 F (2d) 995 (CCA 3rd, 1933), cert. den. 291 U. S. 660, 78 L. Ed. 1052, 54 S. Ct. 377 (1934); *Levy's Estate* v. *Comm.*, 65 F (2d) 412 (CA 2nd, 1933).

The 1939 Code imposes an excise tax

> "upon the transfer of the net estate." (Sec. 810.)

The net estate is determined by deducting certain items from the gross estate. (Sec. 812.) The gross estate is determined by

> "including the value at the time of his (decedent's) death of all property * * * (Sec. 811);
>
> "To the extent of the *interest therein of the decedent at the time of his death* (Sec. 811(a)), (Br. 2, *supra.*)
>
> * * * *
>
> "To the extent of *the amount receivable by the executor* as insurance under polices upon the life of the decedent. (See 811(g)(1);
>
> "To the extent of *the amount receivable by all other beneficiaries* as insurance under policies upon the life of the decedent * * *." (Sec. 811(g)(2)). (*Italics supplied.*) (Pet. Br. 43.)

Analysis of these provisions indicates that Congress did not consider that the proceeds of life insurance rep-

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[2] The Tax Court continues to hold to the contrary notwithstanding reversals by Courts of Appeals. (R. 14.)

resented an interest of the decedent at the time of his death, otherwise they would have been covered by Sec. 811(a), and it would not have been necessary to include them specifically in Sec. 811(g)(1) and (2). This conclusion is confirmed by the omission from Sec. 811(g)(1) and (2) of the language "the interest therein of the decedent at the time of his death" contained in Sec. 811(a) and the substitution of the words "the amount receivable by the executor (all other beneficiaries) under policies upon the life of the decedent."

The distinction between the interest of the insured in property at the time of his death and the interest of the beneficiary in proceeds of insurance was recognized in *John Hancock Mutual Life Insurance Co.* v. *Helvering*, 128 F(2d) 745, 746 (CA D.C., 1942), involving a lien for estate taxes imposed by Sec. 315(b), Rev. Act of 1934, corresponding to Sec. 827(b), I.R.C. of 1939. In its opinion the Court said:

> "The imposition of liability appears to follow two lines. First is the case where decedent makes a *transfer* by *trust* or otherwise. Second is the case where *insurance passes* under a contract to a specific *beneficiary*. These two cases are set off by '(1)' and '(2)'. If the tax has not been paid, it is provided that in *either case* the *transferee, trustee,* or *beneficiary* is personally liable. The statute proceeds to impose a lien on the estate *property* to the extent of *decedent's interest* at the time of *transfer* or to the extent of the *beneficiary's interest* under the *insurance* contract. (*Italics the Court's*).

The quotation from the opinion of this Court in *Chase National Bank* v. *U. S., supra,* (Pet. Br. ~~13~~, 14), shows that the estate tax is not imposed upon the transfer of the proceeds to an individual beneficiary *as the property of the decedent:*

> "Termination of the power of control at the time of death inures to the benefit of *him who owns the property subject to the power* and thus brings about

at death the completion of that *shifting of the economic benefits* which is the real subject of the tax, just as effectively as would its exercise, which later may be subjected to a privilege tax." (*Italics supplied.*)

Other instances where Congress has brought within the purview of the estate tax law property which does not belong to the decedent at the time of his death are irrevocable *inter vivos* transfers made in contemplation of death or intended to take effect in possession or enjoyment at or after death (Sec. 811(c)); revocable transfers (Sec. 811(d)); and transfers of property held as joint tenants or as tenants by the entirety. (Sec. 811(e).) Certainly up to the time of death the decedent has it within his power to revoke a revocable transfer and to sell his interest in a joint tenancy no less than his power to revoke the beneficiary of his life insurance policy.[3]

It has been held that decisions of this Court such as *Tyler v. U. S.*, 281 U. S. 497, 74 L. Ed. 991, 50 S. Ct. 356 (1930), *Phillips* v. *Dime Trust & Safe Deposit Co.*, 284 U. S. 160, 76 L. Ed. 220, 52 S. Ct. 46 (1931), and *Gwinn* v. *Comm.*, 287 U. S. 224, 77 L. Ed. 270, 53 S. Ct. 157 (1932), upholding the estate tax upon the transfer of the interest of a decedent in a tenancy by the entirety or in a joint tenancy, are not precedents for the determination of whether his interest therein is his property *within the meaning of Sec. 311(a)(1)*; and that such an interest does not constitute *property of a taxpayer* within the meaning of that section. (*Irvine* v. *Helvering*, 99 F (2d) 265, 270, (CCA 8th, 1938); *Tooley* v. *Comm.*, 121 F (2d) 350, 354, (CCA 9th, 1941); *Parker* v. *Comm.*, 122 F (2d) 230 (CCA 9th, 1941); *U. S.* v. *Hutcherson*, 188 F (2d) 326 (CA 8th, 1951).

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[3] Petitioner admitted in his petition for certiorari that the bonds and real estate held in the joint names of decedent and respondent with right of survivorship were "not available for the payment of taxes," referring to decedent's unpaid income taxes. (Pet. 3.)

A priori the decisions of this and other Courts in *Chase National Bank* v. *U. S.*; *Heiner* v. *Grandin*, *Cook* v. *Cook*, and *Levy's Estate* v. *Comm.*, *supra*, relied upon by petitioner, (Pet. Br. 13-15), are not apposite to the question of whether proceeds of insurance are property of a taxpayer within the meaning of Sec. 311(a)(1).

2. *Respondent Is Not A Transferee Of The Property Of The Decedent With Respect To The Proceeds.*

If the proceeds of insurance were not the property of the decedent during his lifetime, then it follows that respondent is not a transferee of property of the decedent with respect to the proceeds.[4] Nor was she a transferee of property of the decedent's estate, as the proceeds were not payable to his estate and never belonged to it. This was the decision of all of the Courts of Appeals which have considered the question. (*Stern* v. *Comm.*, R. 17; 242 F (2d) 322 (CA 6th, 1957); *Tyson* v. *Comm.*, 212 F (2d) 16 (CA 6th, 1954) *Rowen* v. *Comm.* 215 F (2d) 641 (CA 2nd, 1954); *U. S.* v. *New*, 217 F (2d) 166 (CA 7th, 1954); *U. S.* v. *Truax*, 233 F (2d) 229 (CA 5th, 1955); *U. S.* v. *Bess*, 243 F (2d) 675, 678 (CA 3rd, 1957).)

The Court of Appeals for the Second Circuit in the *Rowen* case, *supra*, answered the question as to whether a beneficiary of a life insurance policy is a transferee of the proceeds as follows:

> "Were the beneficiaries of the policies here involved 'transferees' with respect to *the proceeds of the poli-*

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[4] The substance of petitioner's argument that decedent is a transferor of the proceeds is that he could have changed the beneficiary of his policies to his estate and thereby subjected the proceeds to the claims of his creditors. Failure to act does not constitute a voluntary transfer of property to defeat the claims of creditors. (*Tyson* v. *Comm.*, 212 F (2d) 16, 17.) This should be all the more true here, where the policies were taken out many years before the Government's claim for delinquent income taxes arose, and where respondent was named the beneficiary at various times ranging from 14 to 30 years before decedent's death.

cies? We think not. In no sense were the *proceeds* ever property of the decedent-taxpayer. Under the policy contracts the decedent never had a right to receive the proceeds. And since at his death the policies were not payable to his estate, the *proceeds* of the policies never passed to his estate and *as to the proceeds* the beneficiaries did not take as legatees or distributees of his estate." (215 F (2d) 641, 644.) (*Italics the court's.*)

This conclusion was concurred in by the Sixth Circuit (*Stern*, R. 17, 19, 242 F (2d) 322, 324), by the Fifth Circuit (*Fraux*, 223 F (2d) 229, 231), by the Seventh Circuit (*New*, 217 F (2d) 166, 167), and by the Third Circuit (*Bess*, 243 F (2d) 675, 678). Moreover, in the *Bess* case the Third Circuit explained that its decision in *Pearlman* v. *Comm.*, 153 F (2d) 560 (1945), should not be construed as holding that an individual beneficiary of a life insurance policy is a transferee of the proceeds, as some Courts had interpreted it.

Of course, if proceeds of insurance are made payable to the insured's estate, they are subject to the claims of his creditors, irrespective of whether they are held by the executor, (*Bank of Minden* v. *Clement*, 256 U. S. 126, 65 L. 857, 41 S. Ct. 408 (1921)), or distributed by the executor to the heirs, (*Kieferdorf* v. *Comm.*, 142 F (2d) 723 (CCA 9th, 1944), cert. den. 323 U. S. 733, 89 L. Ed. 588, 65 S. Ct. 69). Pet. Br. 21.) This is not because they are proceeds *qua* proceeds, but because they are assets of the decedent's estate the same as any other property belonging to the estate.

POINT II

Respondent Is Not A Transferee of the Cash Surrender Values

Whether respondent is a transferee of the cash surrender values of the policies as of the date of decedent's

death likewise depends upon (1) whether they were the "*proprty of a taxpayer*" during his lifetime, and (2) if so, whether respondent is a *transferee* thereof *within the* meaning of Sec. 311(a)(1).

1. *The Cash Surrender Values Were Not the Property of the Decedent*

Petitioner argues that the "Court below erred in holding that the cash surrender values were not assets of the decedent during his lifetime." (Pet. Br. 22.)

The laws of the various states require insurance companies doing business within their borders to maintain reserves for solvency purposes so that they will be financially able to pay the death benefits when the policies mature. Reserve funds and the cash surrender values are explained in Krueger and Waggoner, "The Life Insurance Policy Contract," 1953 Edition, published by The American Society of Chartered Life Underwriters, as follows:

> "In the level premium system of life insurance the net level premium[5] must be higher than the monetary value of the annual risk during the early policy years, and the excess must be accumulated with interest to provide funds for payments of claims after the age is reached where the value of the annual risk exceeds the net level premium in the annual premium being paid. It is the necessary accumulation of these funds that makes possible non-forfeiture benefits. On surrender of a policy the insurer, being relieved of the obligation to provide death benefits

[5] "The net level premium is the annual amount which at the date of issue has a present value just equal to the then present value of insurance benefits to be provided by the policy when the present values are computed on the basis of the mortality table and rate of interest to be used for reserve valuation purposes. The actual annual premium charged the policyholder is referred to as the 'gross premium,' being the net level premium plus a level annual amount for taxes, company expenses and contingencies."

during future years where the annual value of the risk exceeds the annual net level premium, no longer needs to retain the surrendering policyholder's contributions to the funds previously accumulated for such purpose. Since the surrendering policyholder made a contribution to these funds during the period from date of issue to date of surrender, he is *equitably* entitled to a return *equal to the prorata share* of the funds actually accumulated *from premiums paid by his group of policyholders* and no longer needed to assure solvency of the company for the protection of continuing policyholders." (P. 194.) (*Italics supplied.*)

From the above it is clear that a special reserve fund is not maintained for each policyholder. MacLean on "Life Insurance", Eighth Edition, 1957, makes the following statement regarding the integrated nature of reserve funds:

> "While the reserve *per policy* can be arrived at in the manner just described, it is important to realize that such a figure has no real significance as applied to an individual policyholder but is merely an *average* or *factor* to a large number of policies or to a large amount of insurance.[6] * * * It is necessary for some purposes (such as the calculation of cash surrender values) to consider the reserve for an individual policy as being the pro rata part of the total reserve for all similar policies, thus ignoring possible differences in health and probable longevity." (P. 117.) (*Italics the author's.*)

The premiums paid by the insured represent the consideration passing to the insurance company for its promise to pay the proceeds to the beneficiary upon the insured's death. The premiums do not belong to the insured; they belong to the company. Inasmuch as the

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[6] The same author prints the Commissioner's 1941 Standard Ordinary Mortality Table (C.S.O. Table), which is based on 1,000,000 lives. (P. 78). The mortality table is the basis for determination of the net level premium and the reserve.

excess of the net level premiums over the current cost of mortality, together with interest thereon, constitute the reserve fund; it follows that the reserve fund belongs to the company and not to the insured; and, *a priori,* that the cash surrender value belongs to the insurance company, inasmuch as only upon surrender of his policy is the policyholder equitably entitled to a proratable part of the reserve fund.

A few examples will demonstrate that the insured does not own the cash surrender value. If he were to borrow on the security of his policy, the amount of which would reduce the cash surrender value, he would have to pay interest on the loan. Clearly he would not have to pay interest on his own money. If he were the owner of the reserve fund of which the cash surrender value is a proratable part, he would have to pay an income tax on the interest which is accumulated in the fund. The interest, of course, belongs to the insurance company and not to the insured.

Inasmuch as there is a consideration for the promise of the insurance company to pay the proceeds to the beneficiary upon the death of the insured—the promise of the insured to pay the premiums at the time they become due; so, also, is there a consideration for the payment of the cash surrender value of the policy to the insured—the release of the company from its obligation to pay the proceeds to the beneficiary by the insured's surrendering the policy for cancellation. The insured cannot possibly own the policy and the cash surrender value at the same time.[7]

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[7] Policyholder actions against life insurance companies for an accounting and distribution of surplus funds have been unsuccessful on the theory that a policyholder has only a contractual right against the company and no right to any particular assets. (*Equitable Life Assurance Society* v. *Brown*, 213 U. S. 25, 47 (1909); *Andrews* v. *Equitable Life Assurance Society*, 124 F (2nd) 788 (CCA 7th, 1941), cert. den., 316 U. S. 682.)

The record shows that the decedent did not surrender his policies for their cash surrender values (R. 14); and, accordingly, the cash surrender values did not belong to him during his lifetime. The only asset which he owned at the time of his death was the policies under which the insurance companies were contractually obligated to pay the proceeds to the respondent.

Petitioner cites certain cases arising under the Bankruptcy Act as supporting his contention that the insured owns the cash surrender value of a life insurance policy during his lifetime; viz., *Cohen* v. *Samuels*, 245 U. S. 50, 62 L. Ed. 143, 38 S. Ct. 36 (1917), *Hiscock* v. *Mertens*, 205 U. S. 202, 211, 212, 51 L. Ed. 771, 27 S. Ct. 423 (1907), *Burlingham* v. *Crouse*, 228 U. S. 459, 469, 57 L. Ed. 920, 926, 33 S. Ct. 564 (1913). (Pet. Br. 21, 23, 40.) The Bankruptcy Act involved provided that there should devolve upon the trustee all powers with respect to property which the bankrupt himself might have exercised for his own benefit.[8] This Court held that the power to surrender a life insurance policy for its cash surrender value was a power with respect to property which vested in the trustee under the Act. There is no corresponding provision of Federal law applicable to life insurance policies, which has the effect of constituting the cash surrender values as *property of a taxpayer* within the meaning of Sec. 311.

This Court in *New York Life Ins. Co.* v. *Statham*, 93 U. S. 24, 23 L. Ed. 789 (1876), (Pet. Br. 22, 26), merely held that a forfeiture provision for non-payment of premiums should not be enforced, where the insured who resided in the South was unable to pay the premiums due to the Civil War, and that the company should pay the equitable value of the policy. The value was deter-

[8] The Act also permitted the bankrupt to retain the policy by paying over to the trustee an amount equal to the cash surrender value.

mined to be the difference between the premium payable at the attained age of the insured when the premiums were discontinued and the premium payable at the age when the policy was issued.

U. S. v. Updike, 281 U. S. 489, 494, 74 L. Ed. 984, 50 S. Ct. 367 (1930), (Pet. Br. 30, 32), involved the question of whether the statute of limitations applicable to transferees in Sec. 280 or the general statute applicable to taxpayers in Sec. 278(d), Rev. Act of 1926, applied to a suit in equity to compel the stockholders to pay the unpaid income taxes of a dissolved corporation under the trust fund doctrine. This Court held that the limitations in Sec. 280 applied only to assessment and that Sec. 278(d) governed, as it applied to collection. Speaking of the term "taxpayer" in Sec. 278(d), the Court stated that "it puts no undue strain upon the word 'taxpayer' to bring within its meaning that person whose property, being impressed with a trust to that end, is subjected to the burden." The Court did not hold that a "transferee" within the meaning of Sec. 280 was a taxpayer, a logically the Court could not have so held, as a person cannot be a transferee of property of himself.

Petitioner cited the following cases involving Federal tax liens perfected during the insured's lifetime as authority for the proposition that the insured owns the cash surrender value of his policy during his lifetime, (*U. S. v. Hoper,* 242 F (2d) 468 (CA 7th, 1957), (Pet. Br. 10, 27, 28); *U.S. v. Behrens,* (CA 2nd, 1956), 230 F (2d) 504, cert. den. 351 U. S. 919, 100 L. Ed. 1451, 76 S. Ct. 709 (1956), (Pet. Br. 25, 27); *Knox v. Great West Life Assurance Co.,* 109 F. Supp. 208 (1952), aff'd per curiam, 212 F (2d) 784 (CA 6th, 1954), (Pet. Br. 12, 26, 39); *U. S. v. Metropolitan Life Ins. Co.,* 130 F (2d) 149, (CA 4th, 1958), (Pet. Br. 12, 26); *Kyle v. McGuirk,* 82 F (2d) 212 (CCA 3rd, 1936), (Pet. Br. 26, 39, 40); *Smith v. Donnelly,* 65 F. Supp. 415 (E. D. La., 1946), (Pet. Br. 26);

U. S. v. *Prudential Ins. Co. of America,* 54 F. Supp. 665 (E. D. Pa., 1944), (Pet. Br. 26); *U. S.* v. *Ison,* 67 F. Supp. 40 (S. D. N. Y., 1946), (Pet. Br. 12, 26); *U. S.* v. *Royce Shoe Co.,* 137 F. Supp. 786, (D. N. H., 1956), (Pet. Br. 26); *U. S.* v. *Trout,* 46 F. Supp. 484 (S. D. Calif., 1942), (Pet. Br. 26); *Cannon* v. *Nichols,* (80 F (2d) 934 (CAA 10th, 1935), (Pet. Br. 29, 40).

Under Sec. 3670 the lien is "upon all property and rights to property," and under Sec. 3671 it arises "at the time the assessment list was received by the collector and shall continue until the liability for such amount is satisfied or becomes unenforceable by reason of lapse of time." (Br. 2, *supra.*) It was held in the above cases that the lien attaches to the insured's interest in policies which he has the right to surrender for their cash surrender values, and that it follows the policies even though the assured assigns them or dies subsequent to the time the lien becomes effective. Property subject to a lien pases *cum onere,* (*Burton* v. *Smith,* 13 Pet. 464, 483, 10 L. Ed. 248, 257 (1839), *Michigan* v. *U. S.,* 317 U. S. 338, 87 L. Ed. 312, 314, 63 S. Ct. 302, 303 (1943); and not in the case of a life insurance policy due to the insured's ownership of the cash surrender value or due to the merger of the cash surrender value in the proceeds. In *U. S.* v. *Hoper, supra,* the Seventh Circuit specifically noted the distinction between an action arising under the lien provisions of the Code and Sec. 311, the transferee provision.

The income tax liability of the decedent in the instant case was not determined until 1955, which was between five and six years after his death on June 12, 1949. (R. 11, 16.) No lien could have arisen during his lifetime, as it arises only at the time the assessment list is received by the collector. (Sec. 3671.) The proceeds of insurance vested in the respondent upon the decedent's death, and clearly no lien arose retroactively in favor of the United States, either with respect to the cash surrender values or the proceeds of the policies.

It was not held that the beneficiary of a life insurance policy is a transferee of property of a taxpayer under Sec. 311(a)(1) in *U. S. v. Gilmore*, 222 F (2d) 167, 171 (CA 5th, 1955), (Pet. Br. 11, 29), but on the contrary that the widow beneficiary was liable in her fiduciary capacity as executrix for failing to collect from herself personally the amount of estate taxes allocable to the proceeds of insurance which she received. If she had done so, the general assets of the estate used by her to pay the estate taxes would have been available and adequate to pay the deceased's income taxes.

Although understanding that the decision of The Tax Court was "that petitioner (respondent) was subject to the income tax liability of her deceased husband with regard to the proceeds of the life insurance on the ground that she was a transferee of such proceeds and that the Estate of Milton J. Stern, Deceased, had transferred these proceeds to her," (CA Opinion, R. 17), nevertheless, the Court below passed upon respondent's liability as transferee with respect to the cash surrender values as follows:

> "The cash surrender values were not part of the proceeds of the insurance policies paid to the widow, and to hold otherwise would seem to transform plain language to the advantage of the tax-gathering authority, and to the loss of the widow. The widow did not, in any sense, receive the cash surrender values as a transferee of the estate of her deceased husband. The rights of the parties to this suit, and ~~the rights~~ of all parties concerned in the contract of insurance, depended entirely upon agreements executed between the insured and the insurance companies that it would pay the husband the cash surrender values, only on his demand, in lieu of paying his widow the amount of the policies after his death. If the insured did not demand such payment, the insurance companies were bound to pay the entire proceeds of the policies to the insured's wife, upon his death." (R. 25.)

The Second Circuit in *Rowen* v. *Comm.*, 215 F (2d) 641, 644, 645, 647), (Pet. Br. 25), and the Third Circuit in

U. S. v. *Bess*, 243 F (2d) 675, 676, (Pet. Br. 27), reached a contrary result which seems to be incompatible with their unqualified holding that the proceeds of insurance never belonged to the insured. After definitely holding that the proceeds always belonged to the insurance company and never at any time belonged to the insured, they, nevertheless, held that the cash surrender values belonged to the insured during his lifetime and merged at his death with the proceeds which were paid over to the beneficiary. The effect of this reasoning is that cash surrender values, which are always the property of the insured, merge with the proceeds, which are always the property of the insurance company, and still retain their identity as cash surrender values in the hands of the beneficiary. This seems to produce an incongruous result, and respondent submits that the Second and Third Circuits erred in holding that the insured owned the cash surrender values during his lifetime.

If the decision of the Third Circuit in *Pearlman* v. *Comm.*, 153 F (2d) 560, 562 (1945), be deemed to hold that the beneficiary is liable as transferee for an amount of proceeds equal to the cash surrender value of the policy, respondent submits that the Court erred. In that case the insured changed the beneficiary from his estate to his wife after he became hopelessly insolvent and thereafter continued to pay premiums while he was insolvent. The Court held that this constituted a fraud on the insured's creditors, which rendered the beneficiary liable as a transferee.

In the present case the policies were taken out between 1911 and 1935 and respondent was named beneficiary of the various policies between 1919 and 1935, which was 30 to 14 years, respectively, prior to decedent's death in 1949. (R. 18). There was no evidence or finding that the decedent took out or maintained the policies with intent to hinder, delay or defraud his creditors. (CA Opinion, R. 18). There was no evidence or finding that any pre-

miums were paid on the policies during the years decedent was held liable for income taxes or during any subsequent years prior to his death. As to such evidence, petitioner has the burden of proof (Sec. 1119(a); Resp. Br. 2.)

Petitioner devotes a portion of his brief to an argument predicated upon hypothetical facts, without any evidence whatsoever to support them, and with respect to which the petitioner himself has the burden of proof. (Pet. Br. 28; Sec. 1119(a).) He says that if decedent had honestly reported his income, he could have paid his income taxes; or, if he had honestly reported his income and failed to pay his taxes, the Government could have reached the cash surrender values of his policies during his lifetime. This is, of course, mere speculation. Moreover, it may be stated that the determination of The Tax Court was not made until more than five years after decedent's death, (R. 11, 16), when it was no longer possible for him to explain and possibly to justify his action. In any event, any understatement of income by decedent can have no bearing whatsoever upon the question of *whether respondent is liable as a transferee* for the payment of his income taxes. The only effect it can have is to increase decedent's income tax liability, and, consequently, to increase the *amount* of respondent's liability as a transferee, assuming that she is liable.

2. *Respondent Is Not A Transferee Of Property Of The Decedent With Respect To The Cash Surrender Values*

If the cash surrender values of the policies were not the property of the decedent during his lifetime, then respondent is not "a transferee of the property of a taxpayer," within the meaning of Sec. 311(a)(1). Nor is she "a transferee of the property of a taxpayer," if the estate is deemed to be the taxpayer, for the same reason that the cash surrender values never belonged to the estate. Only two Circuit Courts have decided that a beneficiary of a

life insurance policy is a transferee of the cash surrender values, the Second Circuit in *Rowen* v. *Comm., supra;* although holding that there was *no liability* on the part of the beneficiary, and the Third Circuit in *U. S.* v. *Bess, supra,* and also holding that there *was liability* on the part of the beneficiary. We have discussed these cases above and attempted to demonstrate that these Courts were in error in deciding that a beneficiary is a transferee of the cash surrender values. We submit that the decision of the Court below that a beneficiary is not a transferee of the cash surrender values is correct. (R. 17, 21.)

POINT III

There Is No Liability On The Part Of Respondent As Transferee

Even though respondent be deemed to be a transferee of property of the decedent taxpayer within the meaning of Sec. 311(a)(1), either as to the cash surrender values or as to the proceeds of the policies, still there is *no liability* on her part as a transferee under that section or under any other provision of Federal law. It is respondent's position that it is necessary to look to the law of Kentucky to determine her transferee liability, and that under Kentucky law she is not liable. In any event, petitioner has the burden of proving that respondent is liable as a transferee but has failed to do so.

1. Transferee Status And Transferee Liability Are Not Integrated Questions

Although petitioner admits that Sec. 311 creates no new liability on the part of a transferee of property of a taxpayer with respect to his unpaid income taxes, and that it provides merely a summary method of collecting an existing liability, (*Phillips* v. *Comm.*, 283 U. S. 589, 75 L. Ed. 1289, 51 S. Ct. 608 (1931); H. R. 1, 69th Cong., 1st Sess., CB 1939-1, Part 2, pp. 354, 371; *Leighton* v. *U. S.*,

289 U. S. 506, 77 L. Ed. 1350, 53 S. Ct. 719 (1933)); nevertheless, petitioner argues that transferee status and transferee liability are inseparable; and that transferee liability follows *ipso jure*, if one is a transferee. (Pet. Br. 34, 35.)

Sec. 311 covering income tax transferee liability and Sec. 900 covering estate tax transferee liability, (Pet. Br. 42, 45), were originally incorporated into the Rev. Act of 1926, as Secs. 280 and 316, respectively. Aside from changing the section numbers and amending the paragraph applicable to the statute of limitations, both of these sections have been reenacted without change from 1926 to 1953, with one exception.[9] In 1942 the definition of "transferee" in Sec. 900(e) was amended by adding the words: "and includes a person, who, under Sec. 827(b), is personally liable for any part of the tax." (Barton "Federal Income, Estate & Gift Tax Laws, Correlated," Eighth Ed., pp. 387, 532; Ninth Ed. pp. 562, 1044; Tenth Ed., pp. 644, 767; Eleventh Ed., pp. 389, 522; where the various laws are arranged in parallel columns.)

Reference to Sec. 827(b) discloses that among other persons, a beneficiary of life insurance proceeds, which are includible in the gross estate under Sec. 811(g), is made "personally liable for such tax" to the extent of the value of the proceeds as of the date of the decedent's death." (Pet. Br. 44). The purpose of the 1942 amendment of Sec. 900(e) was not to create a liability on the part of a beneficiary of a life insurance policy for the payment of the estate tax but to subject to the summary process of assessment, collection and payment a beneficiary *who already was personally liable for the tax.*[10]

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[9] Sec. 311(a) has been reenacted in Sec. 6902(a), I.R.C. of 1954, without change.

[10] The forerunner of Sec. 827(b) of the 1939 Code was Sec. 409 of the Rev. Act of 1918, which made a beneficiary of a life insurance policy "personally liable for such tax." Sec. 402(f) of

Sec. 827(b) does not make all beneficiaries of life insurance policies personally liable for the tax, and, *a priori*, Sec. 900(e) does not include all beneficiaries of life insurance policies. It is only beneficiaries of policies the proceeds of which are includible in the gross estate, who are covered by Sec. 827(b) and Sec. 900(e). Beneficiaries of policies not falling within the premium payment or incidents of ownership tests set out in Sec. 811(g)(2) are not liable for any part of the estate tax, and, consequently, they are not within the definition of "transferee" in Sec. 900(e), even since the 1942 amendment.

If Congress had deemed the definition of "transferee" in Sec. 900(e) to be broad enough to include the beneficiary of a life insurance policy, there would have been no need to enlarge the definition in the 1942 amendment. The failure to make a similar amendment to Sec. 311(f) can only be interpreted as an indication of Congressional intent not to subject a beneficiary of a life insurance policy to transferee liability with respect to income taxes. Even then it would have been necessary to create the liability by some provision other than Sec. 311(a)(1).

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that Act provided for the first time that proceeds of insurance should be includible in the gross estate, except there was an exemption of $40,000 in respect of policies made payable to all beneficiaries other than the executor. The beneficiary continued to be personally liable for the tax in every Revenue Act subsequent to 1918; however, it was not until 1942, when the definition of transferree in Sec. 900(e) of the 1939 Code was amended to include a beneficiary, that Congress provided that a beneficiary should be subject to the summary process provided for in Sec. 900(a)(1). (Barton "Federal Income, Estate and Gift Tax Laws, Correlated," Eighth Ed., pp. 490, 491, 530, 531; Ninth Ed., pp., 968, 969, 1002, 1003, 1046, 1047.) This seems to demonstrate conclusively that Sec. 900(a)(1) does not create a liability with respect to estate taxes; and, *a priori*, that Sec. 311(a)(1) does not create a liability with respect to income taxes. In fact there is no provision in the 1939 Code creating a personal liability of a beneficiary for income taxes corresponding to Sec. 827(b) creating a personal liability of a beneficiary for estate taxes.

2. *Income Tax Liability Is Governed By State Law*

Petitioner says that the holding of the Second Circuit in *Rowen* v. *Comm.*, 215 F. (2d) 641, 647, "that the liability of a transferee should be limited by State law is, we submit, erroneous." (Pet. Br. 29.) The language of that Court clearly shows that it did not hold that the liability should be *limited* by State law:

> "The conclusion just reached confronts us with the second question posed above. Granted that the appellants are transferees as to the cash surrender values of the policies, are they under 'liability, at law or in equity' for their decedent's unpaid income taxes? In determining this question we hold that local State law governs. For neither by Section 311 nor by any other Federal statute is *liability* of such a transferee defined. Granted that Congress by specific legislation might have preempted the field, it has not chosen to do so. As a result, when Congress extended its general tax collection procedure to the 'liability' of a transferee, it necessarily must have intended that the existence of liability should be determined by State law. Other than State law, there is no source to which we may look for pertinent authority." (*Italics the Court's*).

To the same effect are *Harwood* v. *Eaton*, 68 F. (2d) 12 (CCA 2nd, 1933), cert. den. 292 U. S. 636, 78 L. Ed. 1489, 54 S. Ct. 715 (1934); *Boltz* v. *Helvering*, 134 F (2d) 538 (CCA 8th, 1943); *U. S.* v. *Truax*, 223 F (2d) 229, 231 (CA 5th, 1955; Mertens "Law of Federal Income Taxation," Vol. 9, Ch. 53, §53.05.

The Third Circuit in *Pearlman* v. *Comm.*, 153 F (2d) 560, 562, and in *U. S.* v. *Bess*, 243 F (2d) 675, 677, held that the liability of a transferee under Sec. 311(a)(1) is to be determined by "general law as declared by Federal courts" and not by reference to the law of the State. The fact that the Court stated that liability was determinable under "general law" clearly indicates that the Court did not consider that transferee liability was created under

Sec. 311(a)(1) or by any other Federal statute. The Court necessarily had in mind the common law as contra-distinguished from statutory law.

It has been well settled that there is no Federal common law. In *Erie Railroad Co.* v. *Tompkins*, 304 U. S. 64, 78, 82 L. Ed. 1188, 1194, 58 S. Ct. 817, 822 (1938), this Court said:

> "Except in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the State. And whether the law of the State shall be declared by its Legislature in a statute or by its highest Court in a decision is not a matter of Federal concern. *There is no Federal general common law.*"[11] (*Italics supplied.*)

To the same effect, see 15 *C. J. S.* 630. In 15 *C. J. S.* 616 it is stated:

> "Equitable principles and rules, as administered in the English court of chancery, in so far as applicable to our conditions, have been adopted as part of our common or unwritten law."

The rule is stated in Title 28, Sec. 1652, U. S. C., Act of June 25, 1948, c. 646, 62 Stat. 944, as follows:

> "The laws of the several states, except where the Constitution or treaties of the United States or Acts of Congress otherwise require or provide, shall be regarded as rules of decision in the Courts of the United States in cases where they apply."

Respondent submits that the determination of the liability of the respondent as a transferee of the property

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[11] Petitioner's note (Br. 36), regarding the Court's reference to "Federal common law," involved a controversy between States, where the law of neither State was applicable. Moreover, it should be observed that the Court enclosed the above words in quotation marks, possibly indicating that they were not used in the sense that there is a Federal common law. This would seem to be a reasonable assumption in view of the Court's express holding in the *Erie Railroad* case that there is no federal common law.

of the decedent taxpayer is governed by Kentucky law, inasmuch as there is no Federal law fixing her liability as a transferee.

3. *Respondent Has No Transferee Liability Under Kentucky Law*

Petitioner's entire argument with respect to the application of State law seems to be that State law cannot *limit* the liability of a transferee of property of a taxpayer with respect to income taxes, whereas, the question is whether State law *fixes* the liability in the absence of any governing Federal law. So the question presented is whether respondent is liable as a transferee under Kentucky law.

Sec. 297.140, Kentucky Revised Statutes (Pet. Br. 46, 47), provides that a policy of insurance for the benefit of a married woman "shall inure to her separate use and benefit * * * independently of her husband or his creditors," subject to the provision that an amount equal to any premiums paid by any person with intent to defraud his creditors, with interest thereon, shall inure to their benefit; and Sec. 297.150 provides that when a policy of insurance is taken out in favor of some person other than the one taking it out, "the lawful beneficiary thereof, other than the person effecting the insurance or his legal representatives, shall be entitled to the proceeds against the creditors and representatives of the person effecting the same," subject to the further provision that the amount of any premiums paid in fraud of creditors, with interest thereon, shall inure to their benefit from the proceeds.[12]

[12] Both of these sections originated as far back as 1893, Sec. 297.140 as Sec. 654 and Sec. 297.150 as Sec. 655. (Carroll's Ky. Stats. (1936) Ed. (1893, c. 243, p. 1257, amending 1893, c. 171, p. 612, Sec. 117; 1893, c. 171, p. 612, Sec. 118.))

In *National Life & Accident Ins. Co.* v. *Walker*, 246 SW (2d) 139, 140, the Court of Appeals of Kentucky stated:

> "Both of the subsections of KRS 297.140 were enacted for the protection of the beneficiary, particularly the family of the insured. The intent of subsection (1) is to provide that the proceeds payable to a married woman shall be *her separate estate* free from debts of her husband, the insured." (*Italics ours.*)

In *Park's Exs.* v. *Parks*, 288 Ky. 435, 440, 441, 156 S W (2d) 480, 483, in a suit by the creditors and executors of the insured to have the Court declare that the proceeds payable to the insured's wife as beneficiary were the proceeds of the estate, the Court of Appeals of Kentucky said:

> "However, calling the right of the beneficiary as only an expectancy is not altogether accurate. Technically it may be regarded as something more. It is a right subject to be defeated by the exercise of the reserved power or the lapsing of the policy. Couch, Cyc. of Ins. Law, Sec 308; 29 Am. Jur. Ins., Secs. 1276, 1315. As stated in Martinelli Cometti, 133 Misc. 810, 234 N. Y. S. 389, 391:
>
> > 'There is no question that an existing beneficiary in the policy of insurance is protected until the conditions imposed by the contract are complied with.'"

It is well settled in Kentucky that under Sec. 297.150, formerly Sec. 655 of Kentucky Statutes, the executor of a named beneficiary who predeceases the insured has a right to the proceeds in the absence of a change in the beneficiary by the insured. (*Neal* v. *Shirley*, 137 Ky. 818, 127 SW 47; *Buckler* v. *Supreme Council*, 143 Ky. 618, 136 SW 1006; *Vaughan* v. *Modern Brotherhood*, 149 Ky. 587, 149 SW 937; *Hall* v. *Ayer*, 105 SW 911, 32 Ky. L. Rep. 291; *Bradley* v. *Bradley's Estate*, 198 SW 905, 907.)

The Sixth Circuit in the instant case discussed the Kentucky law but did not need to reply upon it, in view of the Court's holding that the insured owned neither the cash surrender values nor the proceeds of the policies, and that there was no transfer of property of the decedent taxpayer to the respondent. (R. 22-25.)

Art. 7, Sec. 166, of the New York Insurance Law, which is similar to Sec. 297.150 of the Kentucky Revised Statutes, was construed by the Second Circuit in *Rowen* v. *Comm.*, 215 F. (2d) 641, 649,[13] to declare "a substantive right of the beneficiary to the proceeds and his non-liability to creditors," and the Court rejected the Commissioner's contention that it was an exemption statute. Title 56, Sec. 56-905 of the Georgia Code, Annotated, also similar to Sec. 297.150 of the Kentucky Revised Statutes and Art. 7, Sec. 166, of the New York Insurance Law, was construed by the Fifth Circuit in *U. S.* v. *Truax*, 283 F (2d) 229, 233[14] to create a substantive right in the beneficiary and that it was not an exemption statute.[15] In *U. S.* v. *Ress*, 273 F (2d) 675, 677, the Third Circuit held that under Secs. 28 and 29, Chapter 34, Title 17, of the New Jersey Revised Statutes,[16] the language of which is very similar to the language of Secs. 297.140 and 297.150 of the Kentucky Revised Statutes, the widow beneficiary of the insured had a "vested interest" in the proceeds. The Second Circuit in the *Rowen* case and the Fifth Circuit

[13] Art. 7, Sec. 166, is printed in the margin of the opinion at p. 648.

[14] Title 56, Sec. 56-905, is printed in the margin of the opinion at p. 232.

[15] The decisions of the Second and Fifth Circuits are in effect a recognition of the proposition that a law of the State where the insurance is written is as much a part of the policy as if it were incorporated therein. (Bank of Washington v. Hume, 128 U. S. 195; 29 Am Jur. 197.)

[16] Secs. 28 and 29 are printed in the margin of the opinion at p. 677.

in the *Truax* case held that the beneficiary was not liable as a transferee for the unpaid income taxes of the insured; whereas, the Third Circuit in the *Bess* case held that the widow beneficiary was liable, because transferee liability was determinable under Federal instead of State law.

The question actually resolves itself into the ownership of property, in this case the ownership of the cash surrender values or the proceeds of insurance of the policies on decedent's life. As to the ownership of property, the Federal courts always hold that State law governs. (*Tyler* v. *U. S.*, 281 U. S. 497, 74 L. Ed. 991, 50 S. Ct. 376 (1930); *Warburton* v. *White*, 176 U. S. 484, 496, 44 L. Ed. 991, 50 S. Ct. 376 (1900); *Helvering* v. *Stuart*, 317 U. S. 154, 161, 162, 87 L. Ed. 154, 63 S. Ct. 140 (1942); *Blair* v. *Comm.*, 300 U. S. 5, 9, 81 L. Ed. 465, 57 S. Ct. 330 (1936).)

Respondent, respectfully submits that under Kentucky law the decedent did not own either the cash surrender values or the proceeeds of the policies; that the respondent owned the proceeds; and that she was not liable at law or in equity as a transferee of property of the deceased taxpayer within the meaning of Sec. 311.

4. *Petitioner Has The Burden Of Proving Respondent's Liability As A Transferee*

Although respondent has argued that there is no Federal or State law fixing or determining her liability as a transferee of the proceeds or the cash surrender values of the policies, the burden of proof legally is upon the petitioner to show that respondent is liable as a transferee. Sec. 1119(a) of the 1939 Code specifically provides that in cases before The Tax Court the burden to show that the petitioner before that Court is liable as a transferee of property of a taxpayer is upon the Commissioner. (Res. Br. 2, *supra.*) Accordingly, it is not incumbent upon respondent to show that *she is not liable;* but on the con-

trary the burden falls upon the petitioner herein to prove that *respondent is liable* as a transferee of property of the decedent. Respondent submits that the petitioner has failed to cite any Federal or State law fixing or determining her liability as a transferee with respect to the proceeds or the cash surrender values of the policies of insurance.

POINT IV

Questions Not Presented To Or Decided By The Tax Court Are Not Properly Before This Court

The only question before The Tax Court was whether respondent was liable as a transferee of the *estate of decedent* with respect to the *proceeds* of the policies of insurance. (Deficiency letter, R. 4, 5; Petition, R. 3, 4; Answer, R. 6-8; Reply, R. 9-11); and that is the only question decided by The Tax Court. (R. 15, 16.)

The only question presented to the Court of Appeals below was the same, and the Court of Appeals understood that to be the question. (R. 17, 18.)

This Court has held that a question not presented to The Tax Court should not be passed upon by a Court of Appeals for the logical reason that a litigant is entitled to know the basis of the claim against him (*General Utilities Operating Company* v. *Helvering*, 296 U. S. 200, 80 L. Ed. 154, 56 S. Ct. 185) (1935); and that a question not raised before The Tax Court and the Court of Appeals will not be considered by this Court on certiorari. (*Helvering* v. *Tex Penn Oil Co.*, 300 U. S. 481, 81 L. Ed. 755, 57 S. Ct. 569 (1937); *Helvering* v. *Cement Investors*, 316 U. S. 527, 86 L. Ed. 1649, 62 S. Ct. 1125) (1942).

Respondent submits that the only question properly before this Court is her liability as a transferee of the estate of the decedent with respect to the proceeds of insurance.

CONCLUSION

For the foregoing reasons the judgment of the Court of Appeals should be affirmed.

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